

Message Text

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ACTION EA-14

INFO OCT-01 EUR-25 ISO-00 CIAE-00 DODE-00 PM-07 H-03

INR-11 L-03 NSAE-00 NSC-07 PA-04 RSC-01 PRS-01 SP-03

SS-20 USIA-15 AID-20 COME-00 EB-11 FRB-03 XMB-07

OPIC-12 CIEP-03 LAB-06 SIL-01 OMB-01 AGR-20 CEA-02

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INFO TREASURY DEPARTMENT WASH DC PRIORITY

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AMEMBASSY BONN

AMEMBASSY BRUSSELS

USMISSION EC BRUSSELS

AMEMBASSY THE HAGUE

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AMEMBASSY STOCKHOLM

AMEMBASSY TOKYO

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SUBJECT: SCHMIDT-RUMOR MEETING

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1. SUMMARY. AT MEETING BETWEEN GERMAN CHANCELLOR SCHMIDT AND ITALIAN PRIME MINISTER RUMOR ON AUGUST 30-31 AT BELLAGIO, TWO CHIEFS OF GOVERNMENT DISCUSSED ITALIAN AND GERMAN ECONOMIC SITUATIONS, EC ECONOMIC INTEGRATION, TWIN PROBLEM OF WORLDWIDE INFLATION AND THREAT OF RECESSION AND ITALIAN BALANCE OF PAYMENTS FINANCING NEEDS. MAJOR CONCRETE RESULT WAS ANNOUNCEMENT OF AGREEMENT BETWEEN GERMAN BUNDESBANK AND BANK OF ITALY FOR \$2 BILLION GOLD COLLATERAL LOAN. END SUMMARY.

2. MEETING BETWEEN SCHMIDT AND RUMOR CONCENTRATED LARGELY ON ECONOMIC AND FINANCIAL MATTERS. ITALIANS DESCRIBED ITALIAN FINANCIAL PROBLEMS AND EXPLAINED THEIR EFFORTS TO DEAL WITH CRITICAL INFLATIONARY AND BALANCE OF PAYMENTS PROBLEMS (SEE REFTELS). GERMANS AGREED TO SUPPORT WITHIN EC FURTHER 90-DAY ROLL-OVER OF \$1.9 BILLION EC SHORT-TERM CREDIT WHICH MATURES ON SEPTEMBER 18 AND ACCELERATION OF EC STUDY OF POSSIBLE LONG-TERM EC BORROWING FOR RE-LENDING TO FINANCE MEMBER COUNTRIES' OIL DEFICITS. SCHMIDT AND RUMOR ALSO ANNOUNCED AGREEMENT BETWEEN TWO COUNTRIES' CENTRAL BANKS FOR \$2 BILLION GOLD COLLATERAL LOAN FROM BUNDESBANK TO BANK OF ITALY.

3. GOLD COLLATERAL LOAN WOULD HAVE FOLLOWING FEATURES:
(2) SIMULTANEOUS DEPOSIT OF \$2 BILLION AT BUNDESBANK IN NAME OF BANK OF ITALY AND EARMARKING OF EQUIVALENT AMOUNT OF GOLD IN BANK OF ITALY IN NAME OF BUNDESBANK;
(2) MATURITY OF SIX MONTHS RENEWABLE FOR ADDITIONAL 18 MONTHS FOR TOTAL OF 24 MONTHS, (3) GOLD COLLATERAL OF OVER 500 TONS (OF 2,565 TONS NOW IN BOI RESERVES) TO BE VALUED AT 80 PER CENT OF AVERAGE PRICE IN LONDON MARKET DURING EIGHT-WEEK PERIOD PRIOR TO REQUEST; (4) INTEREST RATE TIED TO 180-DAY US TREASURY BILLS; AND
(5) MINIMUM GOLD PRICE GUARANTEE. LATTER PRICE WOULD BE KEPT SECRET SO AS NOT TO AFFECT PRICE OF GOLD IN FREE MARKET. IN EVENT MARKET PRICE AT TIME OF MATURITY IS LOWER THAN GUARANTEED PRICE, BUNDESBANK WOULD NOT SELL GOLD BUT CREDIT WOULD AGAIN BE RENEWED.
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4. DIRECTOR GENERAL OF TREASURY PALUMBO (WHO ATTENDED SCHMIDT/RUMOR MEETING) TOLD TREASATT SEPTEMBER 2 THAT RUMOR HAD GIVEN SCHMIDT LENGTHY DESCRIPTION OF ITALIAN STABILIZATION EFFORTS AND EXPRESSION OF STRONG DETERMINATION OF GOI TO PURSUE STABILIZATION POLICIES. ITALIANS MADE CLEAR THAT THEY DID NOT CONSIDER RECENTLY APPROVED TAX PACKAGE

AS SUBSTITUTING FOR TIGHT CREDIT, BUT AS COMPLEMENTARY TO IT. FURTHERMORE, SERIOUS EFFORT WOULD HAVE TO BE MADE TO REDUCE PUBLIC EXPENDITURES. BOTH PARTIES EXAMINED WORLD-WIDE PROBLEM OF INFLATION AND AGREED ON NEED TO COMBAT IT. BUT, BOTH GERMANS AND ITALIANS WERE ALSO CONCERNED THAT THESE EFFORTS NOT OVERSHOOT THE MARK AND RESULT IN WORLD-WIDE ECONOMIC RECESSION. PALUMBO SAID SPECIFICALLY THAT BOTH GOVERNMENTS WELCOMED US ANTI-INFLATIONARY PROGRAM BUT HOPED THAT IT WOULD NOT BE CARRIED TO EXTREME OF LEADING US AND OTHER COUNTRIES INTO RECESSION.

5. DISCUSSION OF ACCELERATION OF EC STUDY OF POSSIBLE LONG-TERM EC LOAN DID NOT GO MUCH BEYOND EARLIER TALKS BETWEEN FINANCE MINISTERS APEL AND COLOMBO. HOWEVER, BOTH SIDES WISHED TO DOWNPLAY SOMEWHAT POSSIBLE SIZE OF EC LOAN, WHICH THEY THOUGHT HAD BEEN EXAGGERATED IN PRESS REPORTS. (ITALIAN PRESS HAS CITED LOAN OF 3,000-3,500 BILLION LIRE OR ABOUT \$4.5 TO 5.5 BILLION.) ALTHOUGH INTENT OF NEGOTIATING LOAN WOULD BE TO RECYCLE OIL DOLLARS FROM OIL PRODUCERS TO EC MEMBERS, IT WAS PROBABLE THAT THIS WOULD BE ACCOMPLISHED WITH HELP OF CONSORTIUM OF EUROBANKS. PALUMBO SAID GERMANS FAVORED IMMEDIATE DEPOSIT OF \$2 BILLION IN FAVOR OF BANK OF ITALY (RATHER THAN LINE OF CREDIT TECHNIQUE), POSSIBLY FOR REASONS OF DOMESTIC MONETARY POLICY. WHEN ASKED IF GERMANS AND ITALIANS CONTEMPLATED FURTHER GOLD COLLATERAL LOANS, PALUMBO SAID THAT IF ITALIAN BALANCE OF PAYMENTS IMPROVED SUFFICIENTLY THIS WOULD BE BOTH FIRST AND LAST SUCH LOAN. VOLPE

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